



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

Through Courier

Before The Director/HOD (MSCID)

In the matter of Show Cause Notice issued to

Invest Capital Markets Limited

Date of Hearing:

December 30, 2011

Present at the Hearing:

Representing Invest Capital Markets Limited

- i) *Mr. Mehmood Mandiwalla*
- ii) *Ms. Sana Iftikhar*
- iii) *Shahrukh Naqvi*

Legal Counsel, Mandviwalla & Zafar
Legal Counsel, Mandviwalla & Zafar
Head of Equity Sales,
Invest Capital Markets Limited

Representing Invest Capital Investment Bank Limited

- i) *Mr. Khurshid Malik*

CEO, Invest Capital Markets Limited

Representing Faysal Bank Limited

- i) *Mr. Enam Khan*

Head of Equity & Capital Markets,
Faysal Bank Limited

Assisting the Director/ HOD (MSCID)

- i) *Ms. Tayyaba Nisar*

Assistant Director

ORDER

1. This order shall dispose of the proceedings initiated through Show Cause Notice bearing No. MISC/MSW/SMD/1(5)2004 dated December 22, 2011 ("SCN") issued by the Securities and Exchange Commission of Pakistan ("Commission") under Brokers and Agents Registration Rules, 2001, ("the Brokers Rules") to Invest Capital Markets Limited ("the Respondent").
2. The brief facts of the case are that the Respondent is a member of Karachi Stock Exchange (Guarantee) Limited ("KSE") and is registered with the Commission under the Brokers Rules. After perusal of Karachi Automated Trading System ("KATS") data and Off-Market data of KSE dated June 28, 2011, it was observed that unusually high volume in the scrip of Nestle Pakistan Limited ("NESTLE") was traded at KSE. On further scrutiny of the matter, it was revealed that



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the Respondent executed orders of its clients namely Faysal Bank Limited (“FABL”) and Invest Capital Investment Bank Limited (“ICIBL”) in the scrip of NESTLE in a manner whereby FABL sold 4,707 shares and 3,200 shares to ICIBL at 03:24 pm and 03:25 pm respectively at the rate of Rs. 5,200 in the Ready Market and bought the same from ICIBL at the rate of Rs. 5,203.60 at 03:36 pm in the Off-Market, hence, resulting in no change in the beneficial ownership of the shares. The trading summary for the said transactions is presented below:

Ready Market (June 28, 2011)						
Name	TRADE DATE	TRADE TIME	TRADE PRICE	QTY	B_S	COUNTER PARTY NAME
Faysal Bank Limited	20110628	1524550002	5,200.00	4,707	S	Invest Capital Investment Bank Limited
Faysal Bank Limited	20110628	1525170002	5,200.00	3,200	S	Invest Capital Investment Bank Limited

Off - Market (June 28, 2011)						
Name	TRADE DATE	TRADE TIME	TRADE PRICE	QTY	B_S	COUNTER PARTY NAME
Faysal Bank Limited	20110628	1536067500	5,203.60	4,707	B	Invest Capital Investment Bank Limited
Faysal Bank Limited	20110628	1536229218	5,203.60	3,200	B	Invest Capital Investment Bank Limited

3. It was observed that trades executed between FABL and ICIBL in the Ready Market contributed 99% of the total volume of 7,982 shares in NESTLE on the said date and were executed at day’s high price. Moreover, the said transactions created artificial volume in the market in the scrip of NESTLE, as there was no change in the beneficial ownership.
4. In view of the above, the Commission inquired from the Respondent vide letter dated August 04, 2011 to provide its comments and explain the rationale behind the execution of the trades in question. The Respondent vide its letter dated August 08, 2011 replied that being corporate member of KSE, the trading in the scrip was executed by it on the instructions of its clients, FABL and ICIBL. The Commission vide its letter dated August 12, 2011 again inquired the Respondent to provide the explanation regarding the execution of the trades in question as per Clause 19 (a) of the KATS Regulations of KSE, the broker is deemed responsible for scrutinizing validity and genuineness of each and every transaction executed through its terminals. The Respondent vide its letter dated August 24, 2011 reiterated its stance and narrated that since NESTLE is a thinly traded scrip and few trades in the scrip contribute to the high volume of the scrip. Further, the Respondent stated that it facilitated the Off-Market reversal of the said trades keeping in view that its clients might want to change the investment classification of the scrip.



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5. In this regard, the Commission also inquired FABL vide letters dated July 14, 2011 and August 12, 2011 regarding the execution of the trades in question. FABL presented its response vide letters dated July 28, 2011 and August 24, 2011 whereby it submitted that FABL is an active market participant and it was the responsibility of the Broker to intimate FABL if the transactions in question were in contrast with any regulatory provisions.
6. In light of the aforementioned, the SCN dated December 22, 2011 under the Brokers Rules was issued to the Respondent. The Respondent was asked to submit a written reply within seven days of the date of SCN and hearing was fixed on December 30, 2011 at Commission's Karachi office. Further, the clients of the Respondent namely FABL and ICIBL were also advised to attend the hearing in the said matter.
7. The Respondent submitted its written response to the SCN dated December 29, 2011. The important contentions raised in the response are reproduced hereunder:
 - i. *It is respectfully submitted that the term "Wash Trade" has been defined in the report of Task Force: Review of Stock Market Situation, 2005 of the Securities and Exchange Commission of Pakistan, as follows:*
"A wash trade is an illegal stock trading practice whereby an investor simultaneously buys and sells shares in a company through different brokers. Such a trade enhances the activity in the stock, giving the impression of active trading without any change in beneficial ownership, a clear violation of Section 17 of the Securities and Exchange Ordinance, 1969." (Emphasis Added)
 - ii. *Furthermore, the Black's Law Dictionary (Seventh Edition), not only characterizes such activity as "sale of securities made at about the same time as purchase of the same securities, resulting in no change in beneficial ownership", but at the same time emphasizes that "securities laws prohibit a wash sale made to create the false appearance of the market activity". (Emphasis Added)*
 - iii. *The Transactions have not been executed by Faysal Bank Limited "through two different brokers". Additionally, as noted above, "intention" to create such a false impression is prerequisite for establishing a wash trade; however, there is no evidence to suggest that the Transactions were executed by InvestCap with intent to create a false impression and/or artificial volume in the market.*



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- iv. *Also, the Transactions have been duly settled by InvestCap through National Clearing Company of Pakistan which substantiates that the Transactions have only resulted in change in beneficial ownership.*
- v. *It is respectfully submitted that the scrip of Nestle are not actively traded and thereof, it is usual that a few trades in the scrip contribute to large part of its volume.*
- vi. *It is also further submitted that the Transaction took place at 3:24 pm and 3:25 pm, merely 5 to 6 minutes before closure of the Karachi Stock Exchange. Therefore, even if the Transactions resulted in creation of artificial volume/ contributed to 40 points in the index, the same neither resulted in increased trade in scrips of Nestle nor was any false sentiment created on KSE 100 Index as the Karachi Stock Exchange closed within 5 to 6 minutes of the Transaction taken place.*
- vii. *It is further submitted that a pre-requisite to establish liability under Section 22 of Securities and Exchange Ordinance, 1969, the element of "willful act" and the "intention" is essential to be proved.*
- viii. *The Transactions were executed by InvestCap on instructions of its clients Faysal Bank in "good faith" and that InvestCap had at no instance, knowledge or intent to create a false impression and/or artificial volume in the market.*
- ix. *Creation of false impression and/or artificial volume in the market as a result of the Transactions is accidental and thereof, execution of the Transaction by InvestCap does not come within the purview of Section 22 of the Ordinance.*

8. Subsequently, the hearing in the matter was held on December 30, 2011. The hearing was attended by Mr. Mehmood Mandiwalla and Ms. Sana Iftikhar ("**Legal Counsel of the Respondent**"), Mr. Enam Khan ("**Representative of FABL**"), Mr. Khurshid Malik ("**Representative of ICIBL**") and Mr. Shahrukh Naqvi ("**Representative of the Respondent**").

(A) The Legal Counsel of the Respondent at the time of hearing reiterated the contentions made in the written response. Further, the following submissions were made verbally:

- i. *The Transactions don't fall under the ambit of Wash Trades keeping in view the definition presented in report of Task Force: Review of Stock Market Situation, 2005 of the Commission, which can be confirmed from the following:*



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- a. *There was a change of beneficial ownership for the trades in the question, as there was proper settlement of the shares traded with National Clearing Company of Pakistan Limited.*
 - b. *There were no two brokers involved in the Transaction.*
 - c. *There was no intention to create false market.*
- ii. *The Transactions were executed within last 5 minutes to the closure of market which in anyway could not create false/ misleading impression.*
 - iii. *The Transactions were executed in order to facilitate the client FABL, therefore, the parent company of the Respondent namely ICIBL acted as counter party of the FABL in the Ready Market as well as Off-Market.*
 - iv. *The Legal Counsel prayed that keeping in view the aforementioned arguments the Commission may take a lenient view in the matter.*

(B) The Representative of FABL presented the following submissions:

- i. *The Bank inherited the portfolio of National Investment Trust Limited ("NIT") in January 2010. The bank has been focused on divesting the NIT Portfolio to bring the total investment book of the Bank in-line with the limit of 30% prescribed by the Regulation 6 of Prudential Regulations of SBP.*
- ii. *The SBP had exempted FABL for the said regulation till December 31, 2010 for the portfolio inherited by NIT. However, the Bank was unable to divest the NIT portfolio and had requested SBP for further extension in the exemption till December 2011.*
- iii. *All such Transactions including the trades in question were part of bank's strategy to divest/ shift NIT's portfolio to avoid breach of Prudential Regulations of SBP.*

(C) The Representative of ICIBL presented the following submissions:

- i. *The Transactions were executed in good faith and without any intention to manipulate the market price of the scrip of NESTLE or act in contravention with rules and regulations. However, we assure our complete commitment to abide by all the applicable laws and regulations.*

9. Subsequent to hearing, the Respondent vide its letter dated January 03, 2012 reiterated its contentions submitted during the hearing. Further, it also pledged that as per advice of the



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Commission any such transactions in future would be executed through Negotiated Deal Mechanism. In addition, the aforementioned contentions presented by the Representatives of FABL and ICIBL during the course of the hearing were reiterated vide written responses dated January 09, 2012 and January 11, 2012, respectively.

10. I have heard the arguments of the Respondent and the Representatives of its clients at length during the hearing. Additionally, I have perused the written reply filed by the Respondent and its clients. Accordingly, my opinion on the arguments made by the Respondent, the Legal Counsel of the Respondent and the Representative of the clients to the issues raised in the SCN are as follows:

- i. The contention of the Respondent that there was a change of beneficial ownership is not factually true. The transactions were executed between FABL and ICIBL in the Ready Market, which were reversed between the same clients in the Off-Market, hence no actual change of ownership of the shares took place.
- ii. The Respondent has contended that there was no intent to create false market. It is pertinent to mention that the Respondent has facilitated its clients for transactions which created unusually high volume in the scrip of NESTLE. Although the transactions had been settled through National Clearing Company but the net effect of the transactions was cancelled due to reversal of the transactions in Off-Market.
- iii. The claim of the Respondent that it executed the reversal of the Ready Market transactions between FABL and ICIBL in the Off-Market in order to facilitate its client FABL for change of investment classification of the scrip is not justified. In order to facilitate the clients in the said matter, the Respondent should have executed both the transactions through Off-Market so that such kind of transaction would not impact the market dynamics including movement of KSE – 100 Index.
- iv. The stance of the Respondent that the transactions were executed in the last five minutes and had no impact on the market statistics is denied. The trades in question were last trades of the day in the scrip which contributed in maintaining the closing price of share at high price. Moreover, the price appreciation in NESTLE on June 28, 2011 contributed 40 points in the KSE – 100 Index. It may be noted that NESTLE is a blue chip stock bearing significant weightage in the KSE – 100 Index, any transaction bearing unusual price and volume is likely to impact the Index movement in a significant manner which in turn is vital for driving the market sentiment.



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- v. The Respondent is deemed responsible for the execution of each and every transaction executed through its terminals. It is mandatory for any entity being in the business of brokerage to ensure the validity and genuineness of the trades being executed through its terminals.
- vi. The Respondent showed negligence in conduct of its business for not monitoring the trading activity, which ultimately resulted in false market and unusually high trading activity in the scrip of NESTLE. Being a responsible member of KSE, the Respondent should have conducted its business with due care, diligence and skill.
- vii. The contentions submitted by FABL claiming that transactions were executed following the strategy of the bank to shift/ divest the portfolio inherited by NIT in compliance of Prudential Regulation of SBP, do not justify the execution of trades in question. Being a responsible corporate entity and an active stock market participant, FABL should realize the sensitivity of the transactions and its impact on market dynamics. Any such transaction should have been executed in the Off-Market instead of the Ready Market in order to avoid interference with the smooth operations of the market.
11. After a detailed and thorough perusal of facts, written submissions of the Respondent and its clients and the contentions and averments made by the Respondent and its clients during the course of hearing, it is evident that the Respondent executed trades through its terminals in a manner whereby there was no change of beneficial ownership. The matter was of prime importance keeping in view the sensitivity of scrip of NESTLE in terms of Index weightage and its subsequent impact on the market statistics. The Respondent should conduct its business with responsibility and ensure that full compliance be made of all the rules and regulations of the Commission and stock exchanges. It is the prime responsibility of the Respondent to monitor all trading activities being carried out through its brokerage house and keep track of any transaction which is being made with a view to create any misleading impression.
12. In light of the above facts, I am of the view that the Respondent has not exercised diligence and care while performing its obligations. However, considering the fact that this is the first noted occurrence of such improper practice by the Respondent and the Respondent has assured to adopt cautious approach in future, lenient view in the matter has been taken. Therefore, at this particular instance the Respondent is strictly warned to abstain from any malpractice in future failing which appropriate action will be taken. Further, I also direct the Respondent to ensure that full



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compliance be made of all rules, regulations and directives of the Commission in the future for avoiding any punitive action under the law.

13. Further, I am of the considered opinion that FABL and ICIBL being active and eminent market participants should conduct their trading activities with fairness, prudence and in a judicious manner. Moreover, as the said transactions were specifically initiated upon the request of FABL, it is equally accountable for the impact created by the said transactions on market statistics. Therefore, FABL is reprimanded to refrain from indulging in practices which are in contrast with fair and smooth execution of market operations.
14. This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent and its clients in accordance with law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.



Amran Inayat Butt
Director/HOD (MSCID)

**Announced on January 31, 2012
Islamabad.**

Copy to:

- 1. The President and CEO,
Faysal Bank Limited,
Faysal House, ST-02, Shahrah-e-Faisal,
Karachi.*
- 2. The President,
Invest Capital Investment Bank Limited, C3C,
12th Lane, Ittehad Commercial,
Phase – II Extension, DHA,
Karachi.*